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March 31, 2004

VIA ELECTRONIC SUBMISSION

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, SW – Lobby Level
Washington, D.C. 20554

Re: ***Notice of Ex Parte – CC Docket NOS. 93-193, 94-65, and 94-157***
Verizon Telephone Companies Petition for Reconsideration,
"In the Matter of Stale or Moot Docketed Proceedings"

Dear Ms. Dortch:

SBC submits the following *ex parte* in response to AT&T's March 15 *ex parte* in the above-referenced proceeding. Although AT&T offers no new arguments in its *ex parte*, it has once again presented a specious legal analysis, and it has mischaracterized the record evidence. Accordingly, SBC takes the opportunity to set the record straight.

As an initial matter, what is most notable about AT&T's *ex parte* is that AT&T fails completely to rebut SBC's showing that this investigation does not involve a matter as to which the Commission's rules were silent. To the contrary, AT&T concedes, as it must, that section 65.800 of the Commission's rules *dictated* the manner in which the rate base was to be calculated. That provision stated (and still states) that the rate base "*shall consist of* the interstate portion of the accounts listed in § 65.820 … minus any deducted items computed in accordance with § 65.830." (Emphasis added). Since the Commission held *twice* that, at the time the tariffs at issue here were filed, § 65.830 could not be read to require the deduction of accrued OPEB liabilities, section 65.800 of the Commission's rules did not permit, much less require, LECs to deduct accrued OPEB liabilities in calculating their rate bases.

Unable to dispute SBC's showing that the Commission's rules in 1996 did not permit LECs to deduct accrued OPEB liabilities from their rate bases, AT&T resorts to three arguments. First, it claims that the PCI adjustments at issue were exogenous cost changes resulting from changes in USOA requirements, and, as such, were inconsistent with the 1995 *Price Caps Order*. *AT&T ex parte at 4.* As SBC and others have previously noted, that is a mischaracterization of the PCI adjustments. Those adjustments were not exogenous cost changes to reflect additional OPEB

expense resulting from the accounting changes required by SFAS 106. They were PCI adjustments the sole purpose and effect of which were to *correct errors* in previous tariff filings – specifically, errors in the calculation of the sharing obligations – which were caused by the Common Carrier Bureau's misinterpretation of the Commission's own ratemaking rules. Thus the holding in the 1995 *Price Caps Order* that AT&T cites is inapt.

Second, noting that the Commission's sharing rules contemplate the sharing of "base period earnings," AT&T claims that LECs could at most reverse the OPEB deduction for the 1995 base period rate base, plus possibly restate 1994 sharing obligations based upon "final" rate base figures. *AT&T ex parte at 3-4.* This argument, as well, is flawed. Although AT&T's *ex parte* offers no support for the claim that LECs would be barred from restating their rate base for years prior to 1994, AT&T has previously relied on § 65.600(d) of the Commission's rules in making this claim. But as SBC has pointed out in response to that claim, AT&T misreads § 65.600(d). That provision requires that within 15 months of the end of each calendar year, LECs "file a report reflecting any corrections or modifications to their interstate rate of return," but it does not say that a further restatement is not permitted. Indeed, the latter reading of the rule is not only inconsistent with its text, but patently unreasonable given that the Commission's four year delay in resolving the Applications for Review of RAO 20 made it impossible for LECs to make the necessary corrections to their rate bases in the 15-month report.

While AT&T's attempts to invoke the Commission's rules are thus unavailing, its arguments must fail for another, overriding reason: they rest on the untenable proposition that when Commission staff misapplies the Commission's own ratemaking rules, and the Commission takes four years to correct staff's error, LECs have no recourse. Among other things, that position is flatly inconsistent with the spirit, if not the letter, of the rule against retroactive ratemaking. *See Arizona Grocery Co. v. Atchison, Topeka Santa Fe Railway Co.*, 284 U.S. 370 (1932). Just as the Commission may not order a common carrier to pay reparations for charging a rate that the agency had explicitly approved, neither can the Commission achieve the same practical result by denying a carrier the ability to reverse the effect of a misapplication by Commission staff of the Commission's ratemaking rules. Indeed, when the Commission misapplies its own rules there is a "strong equitable presumption" in favor of putting the parties in the place they would have been had the rules been properly applied in the first place. *Exxon v. FERC*, 182 F.3d 30, 49 (D.C. Cir. 1999); *Verizon Telephone Companies v. FCC*, 269 F.3d 1098, 1111 (D.C. Cir. 2001).

AT&T also claims that the adjustments made to the 1996 access tariffs would grant LECs "a pure windfall at the expense of ratepayers." *AT&T ex parte* at 2. Indeed, it claims "[t[here has never been any dispute in this proceeding with regard to the matter." AT&T is wrong on both counts. As an initial matter, *ratepayers* have nothing to do with this proceeding. AT&T has made no commitment to return money it receives in this proceeding to *ratepayers*. To the contrary, AT&T seeks a windfall to keep for itself. More fundamentally, as SBC has shown, the analysis in *RAO 20* and in the *Report and Order* subsequently requiring LECs to deduct accrued OPEB liability from their rate bases was incorrect. Both of those orders held that accrued OPEB liabilities were analogous to accrued pension liabilities and should therefore be given the same

rate base treatment. But, as SBC pointed out, that analysis was facile and incorrect because, unlike accrued pension expenses, *which were fully recovered from ratepayers as a result of rate of return regulation*, accrued OPEB expenses were *not fully recovered from ratepayers because the Commission denied LEC requests for exogenous cost treatment of such expenses.* Thus, as SBC previously pointed out, to require LECs to deduct accrued OPEB liability from their rate base was a *misapplication* of the principle that rates should not provide a return on zero cost sources of funds.

Pursuant to 1.1206 of the Commission's Rules, this letter is being filed electronically with the Commission.

Sincerely,

/s/ Gary L. Phillips

cc: Tamara Preiss
Jay Atkinson
Aaron Goldschmidt
Jane Jackson
Deena Shetler
Andrew Mulitz
Andrea Kearney
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